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IN THE

Supreme Court of the United States

OCTOBER TERM, 1958

No. 518

THE ATLANTIC REFINING COMPANY,
CITIES SERVICE PRODUCTION COMPANY,
CONTINENTAL OIL COMPANY, AND
TIDEWATER OIL COMPANY,

Petitioners,

v.

PUBLIC SERVICE COMMISSION OF THE
STATE OF NEW YORK,
LONG ISLAND LIGHTING COMPANY, AND
PUBLIC SERVICE ELECTRIC AND GAS COMPANY,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED
STATES COURT OF APPEALS FOR THE
THIRD CIRCUIT

BRIEF FOR PETITIONERS

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March 9, 1959

BORG PRINTING COMPANY OF TEXAS, HOUSTON, TEXAS

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Petitioners,

v.

Public Service Commission of the
State of New York,
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Public Service Electric and Gas Company,

Respondents.

On Writ of Certiorari to the United
States Court of Appeals for the
Third Circuit

BRIEF FOR PETITIONERS

OPINIONS BELOW

The opinion of the Court of Appeals (R. 653) is reported at 257 F. 2d 717. The order of the Federal Power Commission (R. 484), issued June 24, 1957, is reported at 17 F.P.C. 880.

JURISDICTION

The judgment of the Court of Appeals was entered on June 30, 1958 (R. 663). Petitions for rehearing were denied on August 27, 1958 (R. 666-667). The petition for writ of certiorari was filed on November 25, 1958, and was granted on January 12, 1959 (R. 669). The jurisdiction of this Court rests upon 28 U.S.C. 1254(1) (1948) and Section 19(b) of the Natural Gas Act, 52 Stat. 831 (1938), 15 U.S.C. 717r(b) (1952).

STATUTES INVOLVED

This proceeding involves an interpretation of the authority and discretion of the Federal Power Commission under Sections 7(c) and 7(e) of the Natural Gas Act [52 Stat. 825 (1938), as amended, 56 Stat. 83 (1942), 15 U.S.C. 717f(c) (1952), and 56 Stat. 84 (1942), 15 U.S.C. 717f(e) (1952)], and an interpretation of the power of the reviewing court under Section 19(b) of the Natural Gas Act [52 Stat. 831 (1938), 15 U.S.C. 717r(b) (1952)].[1]

QUESTIONS PRESENTED

1. Whether Section 7 of the Natural Gas Act vests the Federal Power Commission with the administrative discretion to certificate sales of gas by independent producers without determining that the proposed initial contract rate is just and reasonable under the standards provided in Sections 4 and 5 of the Act?

2. Whether an applicant's refusal to accept a conditional certificate deprives the Commission of authority, on rehearing, to issue an unconditional certificate?

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[1] For convenience of the Court and in accordance with Rule 40(c) of the Supreme Court Rules, the pertinent portions of the Natural Gas Act are set out in the Appendix hereto, *infra*, pp. 1a-14a.

3. Whether Section 19(b) of the Act precludes a reviewing court from reversing a Commission certificate order on the ground, not urged at any time before the Commission or the court, that the Commission lacked statutory jurisdiction to consider the certificate application because the applicant previously refused to accept a conditional certificate?

STATEMENT

This proceeding involves an order of the Federal Power Commission ("Commission") certificating the sale of natural gas to Tennessee Gas Transmission Company ("Tennessee") by The Atlantic Refining Company, Cities Service Production Company, Continental Oil Company and Tidewater Oil Company ("Producers"),[2] in accordance with the terms of the gas sales contracts between each of the Producers and Tennessee (R. 489). The Court of Appeals vacated the Commission's order upon its *sua sponte* determination that the Commission lacked statutory jurisdiction to grant the certificates (R. 653).

1. Factual Background.

Each Producer owns a 25 per cent interest in gas leases covering about 95,000 acres located in the Gulf of Mexico, 25 to 30 miles offshore Cameron and Vermilion Parishes, Louisiana (R. 25-26, 64, 280). These leases were issued by the State of Louisiana, and have been continued in effect by the Outer Continental Shelf Lands Act [R. 26, Act of August 7, 1953, 67 Stat. 462, 43 U.S.C., 1331-1343 (Supp. I, 1954)]. Continental Oil Company was designated operator of the properties (R. 23). Platforms were constructed in the Gulf of Mexico and wells were drilled and completed (R. 25).

[2] These four independent producers have sometimes been referred to as the CATC or CATCO Companies. However, since each has a separate status and since there is no CATC or CATCO entity, these four certificate applicants are more accurately referred to herein as "Producers".

Each Producer entered into a separate contract to sell its share of the production from the leases to Tennessee (R. 23-25). These contracts provided that each of the parties thereto would file with the Federal Power Commission the necessary applications for certificates of public convenience and necessity, and that such applications would be prosecuted with diligence to the end that certificates would be issued on or before April 1, 1957; and that if any of such applications were denied or if *satisfactory* certificates had not been issued by April 1, 1957, either party could terminate and cancel the contract (R. 28, 287-288).

Under these four contracts, Tennessee acquired a dedication of two trillion cubic feet of natural gas for its system (R. 25). Deliveries to Tennessee under these contracts will approximate 240 million cubic feet of natural gas per day for 20 years (R. 45, 209-210). The initial contract price for such gas is 21.4 cents per Mcf (R. 310, 566).[3] There is no price in the area other than that stipulated by the parties since there were no other sales of gas in the West Cameron, East Cameron and Vermilion offshore areas here involved prior to this sale (R. 43-44). Because the Producers' leases are not in any of Tennessee's Louisiana pricing districts, the proposed sales will not cause economic disruption of existing price structures and will not "trigger" favored-nation or price-redetermination clauses in other contracts (R. 43, 148-159).[4]

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[3] The price of 21.4 cents per Mcf is exclusive of reimbursement for Louisiana gathering or severance taxes. The amount of this tax reimbursement has varied from time to time. At the present time, there is no effective gathering tax reimbursement. The present severance tax reimbursement is 1.5 cents per Mcf. To avoid confusion, prices referred to throughout this brief are exclusive of tax reimbursement.

[4] Typically, favored-nation clauses provide that a purchaser will increase the price paid under contract to equal a higher price paid by that purchaser to another seller within a defined pricing area, or to equal a higher price paid by another purchaser. Price-redetermination clauses typically provide for redetermination of the price paid under contract on the basis of the three highest prices paid in a defined pricing area.

2. Proceedings Below.

During August and September, 1956, the Producers filed applications for certificates of public convenience and necessity requesting authorization for sales to Tennessee in accordance with the terms of their contracts. Respondents, the Public Service Commission of the State of New York ("PSC"), Long Island Lighting Company ("Long Island Lighting"), and Public Service Electric and Gas Company ("Public Service"), intervened in opposition to the proposed sales (R. 330). No evidence was offered by these intervenors.

Tennessee intervened in support of the Producers' applications and adduced evidence showing the advantages which would accrue to it and the public interest from certification of the sales (R. 338-339).

The Presiding Examiner granted certificates to the Producers (R. 498). Upon exceptions to his decision, the Commission issued three successive orders, the last of which is under review. The first order, issued April 22, 1957, granted Producers temporary authority to make the sales, while remanding the proceedings to the Presiding Examiner for further hearing to determine "at what rate the public convenience and necessity" require the sales to be made (R. 519, 523-524). This action was coupled with adoption of the Examiner's findings that such volumes of gas were needed and that the Producers were ready and able to deliver, which findings the Commission held "argue conclusively that the sales are necessary in the public interest" (R. 521).

Because of the unsettled state of the law, particularly with regard to determination of producer rates, the Producers deemed it imprudent to accept the temporary certificates

and filed an application for rehearing (R. 396).[5] Acting upon this application, the Commission issued its order of May 20, 1957 (R. 526). In this order, the Commission referred to the "need for the volumes of gas" mentioned in its April 22 order and decided to issue permanent certificates to the Producers, but reduced the initial contract rates from 21.4 cents per Mcf to 17 cents per Mcf (R. 528, 530).[6] The May 20 order was further conditioned to provide for amendments to the sales contracts enabling the Producers to file applications to increase the 17-cent rate to the original contract rate of 21.4 cents per Mcf. The indicated purpose of the Commission was to fix the initial contract rate at 17 cents and permit the Producers to collect the original initial contract price of 21.4 cents, subject to refund, after the 17 cent price had been effective for one day (R. 528-529).[7] The Producers were afforded thirty days within which to file acceptance of the tendered certificates (R. 532). Before expiration of such thirty-day period, however, they decided that such conditional certificates were not satisfactory and so notified Tennessee (R. 418).

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[5] Because of the possibility of loss of leases and other economic uncertainties inherent in the operations, the final outcome of the certificate proceedings was necessarily a factor of considerable importance to the Producers in determining whether they would commence deliveries in any manner other than under a final certificate, as proposed. Although the Commission had asserted regulatory jurisdiction over Producers' rates following *Phillips Petroleum Company* v. *State of Wisconsin*, 347 U.S. 672, issued June 7, 1954, no criteria for fixing the just and reasonable rates of producers had evolved, or have yet become available. In such circumstances, Producers deemed the uncertainties attendant upon acceptance of the temporary certificates an undue business risk.

[6] In the May 20 order the Commission did not determine the reasonableness of the 17-cent price, but on the contrary, expressly stated that it was not determining that such price "is the proper price under the standards of the Act" (R. 529). Of course, the Commission was not required to make any such determination in this Section 7 certificate proceeding.

[7] Section 4(e), 52 Stat. 822 (1938), 15 U.S.C. 717c(e) (1952), *infra*, p. 1a. Under Section 4(e), the power to order refunds is dependent upon the prior suspension of the increased rate. It should also be noted that an initial rate schedule, such as here involved, "cannot be suspended" by exercise of the powers conferred on the Commission by the Act, as the Commission recognizes in its own Rules [18 C.F.R. 2.4(d), 252].

Faced with the loss of these huge gas reserves, Tennessee filed an application for rehearing of the May 20 order (R. 416). The Commission granted rehearing, heard oral argument and thereafter issued its order of June 24, 1957, which is here under review (R. 424, 484). The June 24 order made clear the Commission's objective to assure commitment of "this great supply" to the interstate market (R. 487). To that end, the Commission decided to postpone a determination of the reasonableness of the initial rate to rate proceedings under Section 5 of the Act, thus according to the certificate proposals here the same treatment it had accorded with regularity to the certificate proposals of other producers. As to three of the Producers, the Commission noted that Section 5 proceedings were already under way and, as to the fourth, it simultaneously instituted a Section 5 investigation (R. 488). "By this means," said the Commission, "relief can be afforded to the consuming public if it should be found that the 21.4-cent initial rate to be charged for offshore gas is excessive" (R. 488). Applications for rehearing of the June 24 order, filed by PSC, Long Island Lighting and Public Service, were denied by order issued August 15, 1957 (R. 447, 458, 466, 541).

Upon petitions for review filed by PSC, Long Island Lighting and Public Service, the Court of Appeals for the Third Circuit vacated the order of the Commission (R. 653). The Court did not decide the case on any issue raised by the PSC, Long Island Lighting or Public Service but, on objection raised *sua sponte*, held that the Commission lacked statutory jurisdiction to consider the Producers' applications because they had indicated an unwillingness to accept certificates containing conditions reducing their initial contract rates (R. 658).

SUMMARY OF ARGUMENT

Three principal points are developed in the Argument. First, under the certificate provisions of Section 7(e) of the Act, the Commission is vested with a broad discretion in considering the various factors which constitute the public convenience and necessity. The Commission's June 24 order, granting the Producers certificates in accordance with their contracts and providing for a determination of the reasonableness of the proposed initial rates in appropriate Section 5(a) proceedings, reflects a proper exercise of this discretion which is adequately supported by substantial evidence. Second, a certificate applicant's refusal to accept a conditional certificate does not deprive the Commission of its statutory jurisdiction, on rehearing, to "change its mind" and issue an unconditional certificate. Thus, the Producers' refusal to accept certificates conditioned on an initial price lower than that stipulated in their contracts did not deprive the Commission of jurisdiction to reconsider their applications and grant them certificates in conformity with their contracts. Finally, the court below exceeded its expressly limited statutory authority by basing its decision on an objection raised *sua sponte*.

Although the Court of Appeals committed substantial error with respect to each of the foregoing points, the main thrust of its decision was a drive toward the imposition of an administrative policy requiring the Commission to determine the reasonableness of initial rates in certificate proceedings — an obvious attempt to substitute its own judgment for that of the Commission. Therefore, the fundamental issue in this case is a determination of the Commission's discretion in a certificate proceeding under Section 7 of the Natural Gas Act. This determination is governed by well-established principles of administrative law, the legis-

lative history of the Act, and the practical problems inherent in proper administration of the Act.

I

The plain language of the Natural Gas Act, its purpose and structure and pertinent legislative history, as well as the Commission's administrative construction of its function thereunder, all support the discretion of the Commission to issue a certificate in accordance with an applicant's contract while providing for a review of the initial rate in a Section 5(a) proceeding.

The Commission's June 24 order certificating the sales proposed by the Producers in accordance with their contracts was a proper exercise of its discretion to evaluate the various elements which comprise that intangible and elusive complex denominated "the public convenience and necessity" and then determine from an analysis of the total situation on which side of the controversy the public interest lies. The factors to be considered and the weight to be given those factors in determining whether an applicant has satisfied the statutory prerequisites are matters within the Commission's discretion, and its judgment will not be disturbed on appeal if supported by substantial evidence. Section 19(b), 52 Stat. 831 (1938), 15 U.S.C. 717r(b) (1952); *ICC* v. *Parker*, 326 U.S. 60, 65 (1945); *SEC* v. *Chenery Corporation*, 332 U.S. 194, 207 (1947); *United States* v. *Detroit & Cleveland Nav. Co.*, 326 U.S. 236, 241 (1945).

Reinforcement of the foregoing principles is found in the legislative history of the Act. As originally enacted, Section 7(c) contained an express statement of Congressional intent that natural gas shall be sold "at the lowest possible reasonable rate consistent with the maintenance of adequate serv-

ice in the public interest." The June 24 order would have met even this restrictive standard, for the Commission took express cognizance of both price and ability to serve. However, the Commission was given far more extensive discretion and control over certificates when Section 7 was amended in 1942 so as to confer broader powers on the Commission which did not limit it to any one criterion or group of criteria. H. Rep. No. 1290, 77th Cong., 1st sess., p. 2 (1941).

Further, in producer-certificate proceedings, the Commission has repeatedly made it clear that, although its determination of public convenience and necessity encompasses a consideration of the initial rate, this is only one of a number of aspects to be weighed. The extent to which and the manner in which consideration shall be accorded to the rate factor are matters charged to the Commission's expertise and discretion based upon the facts of each case.

The Commission's discretion in certificate proceedings is a matter of practical necessity. If the Commission is required in every certificate case to determine whether the proposed initial rate is "just and reasonable" within the meaning of Sections 4 and 5 of the Act, the supply of natural gas available to the interstate market will be severely limited because of the months, if not years, that will elapse before the Commission can determine whether the initial rate sought is justified. The burden on the Commission will become intolerable, and the additional delay between the date of the contract for the sale of natural gas in the interstate market and the time it is certificated will inevitably result in detriment to all parties concerned.

From the language of the Act and the decisions thereunder, it is evident that the Commission has a choice of remedies in treating problems respecting initial rates. As

in this case, the Commission may conclude that the public interest requires immediate issuance of a certificate and postpone determination of the reasonableness of the initial rate to appropriate proceedings under Section 5. Responsibility for selecting the means for achieving the statutory policy and the relation of remedy to policy are matters for the Commission's discretion. *American Power & Light Co.* v. *SEC*, 329 U.S. 90, 112 (1946).

It is for the Commission, not the courts, to evaluate the requirements of public convenience and necessity. *Department of Conservation of Louisiana* v. *FPC*, 148 F. 2d 746 (5th Cir., 1945). This is what the Commission did in its June 24 order, and the benefit that will result to Tennessee and the consumers from an immediate certification of the proposed sales coupled with the uncontroverted evidence that the Producers are able and willing to render the proposed service, provide substantial evidence in support of the Commission's June 24 order.

II

With utter disregard for the Commission's June 24 order and the foregoing principles of administrative law, the Court of Appeals held that the Producers' refusal to accept rate-conditioned certificates deprived the Commission of its "statutory jurisdiction" to consider the certificate applications, and remanded the proceedings with directions to proceed in conformity with its view that the Commission "has left no doubt of the importance and necessity of a consideration of the reasonableness of the proposed initial rate" (R. 659). This the court below did despite the express Commission findings that the need to assure commitment of the gas reserves involved required issuance of certificates in accordance with the Producers' contracts,

and that the consuming public would be adequately protected by postponing inquiry into the reasonableness of the initial rates to proceedings under Section 5(a) (R. 487-488). While expressly recognizing the question of price, the Commission said that, on the facts here, "the precise charge that is made initially is less important than the assurance of this great supply of gas" (R. 487).

The opinion rendered by the court below proceeds upon a manifest misunderstanding of the certificate provisions of the Natural Gas Act and the procedures thereunder. In determining that the Commission lacked authority to reconsider the Producers' certificate applications, the court below erroneously assumed that a certificate applicant merely by filing its application thereby commits itself to undertake service under whatever certificate may issue. This misunderstanding is disclosed by the court's use of the word "threat" to characterize the Producers' refusal of the certificates proffered in the May 20 order. The fallacy inherent in the court's assumption is readily apparent. The court has completely ignored the function that privately negotiated contracts perform in the statutory scheme of regulation. An applicant for a certificate has no obligation or duty, legal or moral, to accept a certificate from the Commission which the applicant feels is unreasonable or otherwise unacceptable; and this is particularly true where, as in the present case, the contracts specifically provide that the certificate must be "satisfactory" to each of the parties. In essence, every applicant requests a certificate exactly as set forth in his application. In this case, it was to make the sales provided for in the Producers' contracts with Tennessee. In the light of *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956), how could the Producers' insistence on certificates in accordance with their contracts deprive the Commission of jurisdiction to

reconsider their applications when those very same contracts formed the basis for the Commission's jurisdiction? Furthermore, an applicant's right to accept or reject a certificate is contemplated by the Commission's regulation,[8] and the legislative history of the Act.

The Commission's authority to reconsider the Producers' applications was firmly established by Section 19(a) of the Act which empowers the Commission "to grant or deny rehearing and to abrogate or modify its orders without further hearing." If, upon reconsidering the certificate applications, the Commission decided to change its mind, it was authorized to do so. *Cia Mexicana de Gas* v. *FPC*, 167 F. 2d 804 (5th Cir., 1948); *National Coal Association* v. *FPC*, 247 F. 2d 86 (D.C. Cir., 1957).

The holding of the court below that the Producers' attempt to obtain certificates in accordance with the terms of their contracts with Tennessee divested the Commission of jurisdiction to reconsider their applications is a blow at the foundation of the regulatory scheme intended by Congress as interpreted in *Mobile*.

III

Reversal of the decision below is independently required because of a plain violation by the Court of Appeals of the express statutory limitation on its reviewing authority.

The court below rejected Respondents' contention that the Commission had abused its discretion. Instead, the court raised an objection not theretofore urged by any party and based its decision solely on a novel question as to whether the Commission had violated its "statutory jurisdiction." The court answered this question in the affirmative, holding

[8] 18 C.F.R. 157.20.

that the Commission lacked authority to consider an application "where the terms of the application limit the scope of the inquiry which the Commission is required to make for a determination of public convenience and necessity" (R. 658).

Section 19(b) of the Act expressly forbids such an approach, for it forecloses judicial consideration of any objection to a commission order "unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do."

This Court and various courts of appeals have strictly applied the foregoing limitation. A reviewing court may not resolve a case on objections raised *sua sponte*, even if it were to apply correct principles in reaching its result. *FPC* v. *Colorado Gas Company*, 348 U.S. 492 (1955). And this rule is applicable even where the issue is one involving the Commission's statutory jurisdiction. *American Power & Light Co.* v. *SEC*, 141 F. 2d 606 (1st Cir., 1944), aff'd, 329 U.S. 90 (1946).

ARGUMENT

The decision of the court below reversing the Commission's June 24 order raises grave questions as to the Commission's authority and discretion under Section 7 of the Natural Gas Act. In particular, the decision below brings into sharp focus questions as to the scope of the Commission's authority to consider a certificate applicant's proposal as submitted, and its administrative discretion to postpone determination of the reasonableness of the proposed initial contract price in order to assure satisfaction of the need for additional supplies of natural gas.

I

THE COMMISSION'S JUNE 24 ORDER WAS A PROPER EXERCISE OF ITS ADMINISTRATIVE DISCRETION WHICH IS SUPPORTED BY SUBSTANTIAL EVIDENCE.

1. Whether A Certificate Application Is in the Public Convenience and Necessity Is a Determination Entrusted to the Commission by Section 7 of the Natural Gas Act.

The Commission's power to grant or deny an application for a certificate of public convenience and necessity is contained in Section 7 of the Natural Gas Act.. Sections 7(c) and 7(e) require the natural gas company to take the initiative and submit its proposal[9]— in this case, the sale of natural gas by the Producers under the terms and provisions of their contracts. Pursuant to these sections of the Act, the Commission is required to issue a certificate if the applicant shows that he "is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Act and the requirements, rules, and regulations of the Commission thereunder," and that such service "is or will be required by the present or future public convenience and necessity." The Producers' applications conformed to this statutory standard, and in its June 24 order, the Commission made both the requisite findings (R. 570). In reaching these conclusions, the Commission showed on the face of its order the considerations which led to its decision. The Commission stated:

[9] We do not understand any party to contend that the Producers did not fully comply with the terms of Section 7(d), dealing with the formal requirements for certificates, or with the Commission's Regulations thereunder. We deal later with the court's holding that the Producers were not willing to comply with the Commission's regulations (*infra*, pp. 33-34).

"In the present status of the case we are left with the difficult problem of how to assure the delivery of this gas to the large market served by Tennessee Gas, and at the same time protect the consumers from an unreasonably high price. In reaching a solution to this problem we are moved by the primary consideration that the public served through the Tennessee Gas system is greatly in need of increased supplies of natural gas. *Further, it appears to us, important as is the issue of price, that as far as the public is concerned, the precise charge that is made initially is less important than the assurance of this great supply of gas.* In view of these circumstances and the fact that the record does not show that the 21.4-cent rate is necessarily excessive, we agree with the presiding examiner that this certificate proceeding under Section 7 of the Natural Gas Act should not assume the character of a rate proceeding under Section 5(a). *We are of the opinion that, in the circumstances of this case, in view of the great demand for gas by customers of Tennessee Gas, the price consideration should not be made the prime determinant of what the public convenience and necessity require.* By virtue of the authority conferred upon us by Sections 4 and 5 of the Natural Gas Act and the proposal to modify the contracts made by the CATCO companies, we are of the opinion that we will be able to adequately protect the public interest with respect to the matter of price. In order, therefore, to insure that deliveries of gas by the four CATCO companies to Tennessee Gas will commence as promptly as possible, we will grant permanent certificates to them by this order without any condition affecting the initial price of 21.4 cents per Mcf" (R. 487; Italics supplied).

The June 24 order clearly demonstrates that the Commission was of the opinion that, so far as the public interest was concerned, the price initially charged for the Producers'

gas was of less importance than the assurance of the great supply of gas. In the exercise of its administrative discretion and expert judgment, the Commission simply found that in view of the great demand for gas by the customers of Tennessee, the price consideration should not be made the prime determinant of what the public convenience and necessity required (R. 487-488). To support its determination, the Commission noted that the record did not show that the 21.4 cent rate was necessarily excessive and that a certificate proceeding under Section 7 of the Natural Gas Act should not assume the character of a rate proceeding under Section 5(a) (R. 487).

The Commission's June 24 order was a proper exercise of its descretion to evaluate the various factors which make up the complex known as the "public convenience and necessity." Having exercised its discretion, the Commission's judgment cannot be disturbed by the reviewing court, absent a showing of abuse of discretion or want of support by substantial evidence.[10] Therefore, it is apparent that the function of the court below was to determine whether the Commission's June 24 order was supported by substantial evidence and not to substitute its judgment for that of the Commission.[11] The mere fact that the court below might have reached a different result would not justify a reversal of the Commission's expert judgment.[12]

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[10] *ICC* v. *Parker*, 326 U.S. 60, 65 (1945); *National Coal Association* v. *FPC*, 191 F. 2d 462, 467 (D.C. Cir., 1951); *Norfolk Southern Bus Corp.* v. *United States*, 96 F. Supp. 756, 761 (E.D. Va., 1950), aff'd, 340 U.S. 802 (1949); *Beard-Laney* v. *United States*, 83 F. Supp. 27, 32 (E.D.S.C. 1949), aff'd, 338 U.S. 803 (1949).

[11] Section 19(b), 52 Stat. 831 (1938), 15 U.S.C. 717r(b) (1952); Administrative Procedure Act, Section 10, Act of June 11, 1946, 60 Stat. 243, 5 U.S.C. 1009 (1952); *SEC* v. *Chenery Corporation*, 332 U.S. 194, 207 (1947); *Willapoint Oysters, Inc.* v. *Ewing*, 174 F. 2d 676 (9th Cir., 1949), cert. den., 338 U.S. 860 (1949).

[12] *United States* v. *Detroit & Cleveland Nav. Co.*, 326 U.S. 236, 241 (1945); *Department of Conservation of Louisiana* v. *FPC*, 148 F. 2d 746, 750 (5th Cir., 1945); *Charleston & Western Caroline Ry.* v. *FPC*, 234 F. 2d 62, 64 (D.C. Cir., 1956).

For if the courts could thus substitute their judgment for the administrative expertise, it would inevitably emasculate the Commission's discretion under the Natural Gas Act and would create an open invitation to administrative chaos.

Even the court below recognized that it is for the Commission, and not the courts, to determine when a certificate of public convenience and necessity should issue, stating (R. 661):

> "The Act entrusts to the Commission, and to the Commission alone, the power and authority to determine the issue of public convenience and necessity. Within the framework of the Natural Gas Act, the Commission alone is entrusted with determining the scope of its inquiry necessary to arrive at the decision of whether to certificate a special sale."

Despite this recognition of the Commission's discretion, the court below would require the Commission, in a Section 7 certificate proceeding, to make a formal determination of whether the proposed initial price is "just and reasonable" under the standards provided in Sections 4 and 5 of the Act. The fallacy inherent in this argument is simply that there is nothing in the Act to require the Commission to make the initial price the prime determinant in resolving the complex of factors it considers in determining the public convenience and necessity. The factors to be considered and the weight to be given to those factors are matters to be determined by the Commission in the exercise of its expert judgment.

The June 24 order clearly evidences that the initial price was one of the factors considered by the Commission in determining that the issuance of a certificate to Producers in accordance with the terms of their contract was required by the public convenience and necessity. The Commission

considered the price factor along with many others, but decided not to make the price the prime determinant nor to convert this certificate proceeding into a formal rate case. In view of all of the circumstances the Commission determined that the public interest would be adequately protected by a review of the initial rates in Section 5(a) proceedings. This was a proper exercise of the Commission's administrative discretion which is sustained by the legislative history of the Natural Gas Act, prior Commission interpretations of its function under Section 7 of the Act, judicial precedent and the exigencies inherent in a proper administration of the Act.

a. *Legislative History.*

As originally enacted in 1938, Section 7 had no provision directly comparable to Section 7(e). Section 7(c) then gave the Commission authority to issue certificates only where it was proposed to render service in an area already being served by another natural gas company. The original Section 7(c) provided:

> "(c) No natural-gas company shall undertake the construction or extension of any facilities for the transportation of natural gas to a market in which natural gas is already being served by another natural-gas company, or acquire or operate any such facilities or extensions thereof, or engage in transportation by means of any new or additional facilities, or sell natural gas in any such market, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require such new construction or operation of any such facilities or extensions thereof; *Provided, however,* That a natural-gas company already serving a market may enlarge or extend its facilities for the purpose of supplying increased market demands in the territory in which it operates.

> Whenever any natural-gas company shall make application for a certificate of convenience and necessity under the provisions of this subsection, the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission. In passing on applications for certificates of convenience and necessity, the Commission shall give due consideration to the applicant's ability to render and maintain adequate service at rates lower than those prevailing in the territory to be served, it being the intention of Congress that natural gas shall be sold in interstate commerce for resale for ultimate public consumption for domestic, commercial, industrial, or any other use at the lowest possible reasonable rate consistent with the maintenance of adequate service in the public interest."

It is noteworthy that, in the concluding directory language expressing the intent of Congress that natural gas should be sold at the "lowest possible reasonable rate consistent with the maintenance of adequate service in the public interest," the Commission was admonished to weigh not only the effect of the rate but also the maintenance of adequate service. Even under this narrow and particularized definition of legislative intent, the June 24 order would be unassailable. For the Commission took express cognizance of both price and ability to serve, concluding finally that the latter would suffer through loss of the reserves, if price were to be emphasized to the exclusion of supply considerations (R. 487).

In 1942, Section 7 was amended to provide the Commission with more extensive certificate control over the transportation and sale of natural gas subject to its jurisdiction. The standards provided by the original Section 7(c) had proven unwieldy in practice.[13] Significantly, the concluding

[13] H. Rep. No. 1290, 77th Cong., 1st sess., pp. 2-3 (1941).

directory provision contained in the original Section 7(c) was deleted, and that restrictive language was replaced by the discretionary authority vested in the Commission by Section 7(e), which confers a broad power on the Commission to scrutinize all aspects of any proposed service. Section 7(e) does not limit the Commission's consideration to any one criterion, or group of criteria.[14] The proper determination and evaluation of the factors constituting the public convenience and necessity were left to the expert judgment of the Commission.

Congress intended for the Commission, not the courts, to delineate the components of public convenience and necessity and to supply its expertise in determining how that standard shall be met in an individual case. The June 24 order rests on the Commission's express conclusion that assurance of supply required postponement of determination of the reasonableness of the initial rate. In holding to the contrary, the court below invaded the province which the legislative history shows Congress intended should be left exclusively to the Commission.

b. *Prior Commission Interpretation and Judicial Precedent.*

Consistent with the broad grant of power under Section 7(e), the Commission has, in practice, asserted discretionary authority in defining the components of public convenience and necessity. Both before and after the 1942 amendment, it resolved the issue of public convenience and necessity by weighing a complex of factors which it enumerated and evaluated.

Whether or not the Commission elects in its discretion to go into the reasonableness of the initial rate in a certifi-

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[14] H. Rep. No. 1290, 77th Cong., 1st sess., p. 2 (1941); Sen. Rep. No. 948, 77th Cong., 2nd sess. (1941), adopting the entirety of the House Report.

cate proceeding, the point is that there is no mandate requiring it to do so.[15] It is for the Commission to say, on a given set of facts, how much importance shall attach to the rate aspect in relation to the other factors which, in the opinion of the Commission, should be considered. *Baltimore & O. R. Co.* v. *United States*, 298 U.S. 349, 358-359 (1936). Often, certificate orders have merely contained a "boiler-plate" provision that they shall not be construed as a waiver of the requirements of Section 4 of the Act and are without prejudice to any findings or orders which have been or may thereafter be made by the Commission in a proceeding pending or thereafter instituted by or against the applicant.[16]

In producer certificate proceedings, the Commission repeatedly has made it clear that, although its determination of the public convenience and necessity encompasses a consideration of the initial contract price, the rate aspect of a producer applicant's proposal is only one of a number of factors to be weighed in the scales of public convenience and necessity. Thus, in denying rehearing in the *Tamborello* case,[17] early in its regulation of producers, the Commission rejected a contention that a proposed sale cannot be held to be required by the public convenience and necessity unless the initial contract rate is found to be "just and reasonable" (15 F.P.C. at 2-3):

> "The Natural Gas Act does not require that each producer-applicant must establish as an indispensable prerequisite to the grant of a certificate of public convenience and necessity to sell natural gas in interstate commerce for resale that the price, terms and condi-

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[15] *Florida Economic Advisory Council* v. *FPC*, 251 F. 2d 643, 646 (D.C. Cir., 1957), cert. den., 356 U.S. 959 (1958); *Oklahoma Natural Gas Co.* v. *FPC*, 257 F. 2d 634 (D.C. Cir., 1958), No. 288, October Term, 1958, pet. for cert. dismissed pursuant to petitioner's motion.

[16] The order under review here contained such a provision (R. 492).

[17] *Re Anthony J. Tamborello, et al.*, 15 F.P.C. 1 (1956).

tions under which such sale shall be consummated shall be the lowest reasonable rate. See *In the Matter of The Atlantic Refining Company*, docket No. G-8809, presiding examiner's decision affirmed December 29, 1955.

"We reaffirm our holding in the order denying rehearing *In the Matters of Cities Service Gas Company and Signal Oil and Gas Company*, docket Nos. G-2569 and G-2570, issued January 15, 1956, that

> 'The rate we deem proper to be charged if a certificate should issue is not necessarily the same we could find to be the lowest reasonable rate under Section 5. Criteria for prescribing a rate necessarily differ from criteria for proscribing a rate.'

"Adoption of the contentions of applicants for rehearing would require that prior to issuance of any certificate of public convenience and necessity authorizing the sale of natural gas in interstate commerce for resale we enter upon the equivalent of a complete Section 5 investigation and, on the basis of the evidence adduced, determine the 'lowest reasonable rate'. The rate so determined would then be imposed by a condition attached to the certificate. Such holding would not only be contrary to the plain language of the act but would also prevent us from exercising the judgment and discretion delegated to us by Congress. Reasonable regulation of natural gas companies, whether interstate pipeline transmission companies or independent producers, requires that our decisions and determinations be the result of a conscientious appraisal of evidence adduced, having regard for the interest of all who may be affected thereby and our determination of the requirements of public convenience and necessity in the circumstances."

In numerous other producer certificate proceedings, the Commission has expressed its judgment that the public interest requires immediate certification to assure maintenance of adequate service and has deferred review of the

initial rates for later proceedings under Section 5.[18] The Commission's long standing interpretation of its function in a Section 7 certificate proceeding and its consistent administration concretely support its June 24 order and are entitled to great weight by the Court in reviewing the validity of that order.[19]

In producer certificate proceedings, the Commission exercises its discretion in light of the particular facts confronting it. An example of this inherent administrative flexibilty is the *Signal* case,[20] decided the same day as *Tamborello*. Because of the circumstances peculiar to the *Signal* record, the Commission attached a condition to the certificate reducing the initial rate from 12 cents per Mcf to 10 cents per Mcf. The rate condition was imposed because the initial contract price of 12 cents per Mcf would "cause economic disruption in a considerable area" (15 F.P.C. at 1021) and because Signal "failed effectively to challenge either the evidence attacking its proposed rate or the evidence supporting the 10-cent rate" (12 P.U.R. 3d at 16).

Assuming *arguendo* that the Commission could properly attach a rate-reducing condition in the *Signal* case, the

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[18] *Re The Atlantic Refining Company, et al.*, Docket Nos. G-8809, et al., order issued December 30, 1955; *Re Alfred C. Glassell, Jr., et al.*, Docket Nos. G-11190, et al., order issued October 18, 1957; *Re Texas Gas Transmission Corporation, et al.*, Docket Nos. G-11965, et al., order issued October 18, 1957; *Re United Gas Pipe Line Company, et al.*, Docket Nos. G-12416, et al., order issued October 29, 1957; *Re Seaboard Oil Company, Operator, et al.*, 19 F.P.C. 416 (1958); *Re Southern Natural Gas Company, et al.*, Docket Nos. G-13864, et al., order issued March 31, 1958; *Re Texas Eastern Transmission Corporation, et al.*, Docket Nos. G-12446, et al., Examiner's Decision issued April 15, 1958; *Re Southern Natural Gas Company et al.*, Docket Nos. G-13082, et al., order issued April 18, 1958; *Re Sunray Mid-Continent Oil Company, et al.*, 19 F.P.C. 618 (1958); *Re The Superior Oil Company et al.*, 19 F.P.C. 637 (1958); *Re United Gas Pipe Line Company, et al.*, 19 F.P.C. 931 (1958); *Re Texas Gas Transmission Corporation, et al.*, Docket Nos. C-14494, et al., order issued August 5, 1958; *Re Transcontinental Gas Pipe Line, Corporation, et al.*, 20 F.P.C. 264 (1958).

[19] *Norwegian Nitrogen Products Co.* v. *United States*, 288 U.S. 294, 315 (1933); *United States* v. *American Trucking Ass'ns.*, 310 U.S. 534, 549 (1940).

[20] *Re Cities Service Gas Company, et al.*, 14 F.P.C. ____, 12 P.U.R. 3d 3, reh. den., 15 F.P.C. 1020 (1955), aff'd, sub. nom., *Signal Oil and Gas Company* v. *FPC*, 238 F. 2d 771, cert. den., 353 U.S. 923 (1956).

rationale of that decision has no application to the present case where the uncontroverted evidence shows that the proposed sales are not in any of Tennessee's Louisiana pricing districts and will not cause economic disruption of existing price structures or "trigger" favored-nation or price-redetermination clauses in other contracts (R. 43, 148-159).

Further, it should be noted that in *Signal* the Commission clearly indicated that it was not determining the reasonableness of the 10-cent rate, stating (12 P.U.R. 3d 16):

> "We wish clearly to state that in conditioning the order to follow to provide for a rate of 10 cents per Mcf, we do not find that this rate is the just and reasonable rate within the meaning of section 4 of the Act."

It merely held that a "vital element" of public convenience and necessity is "concerned with the rates proposed" (12 P.U.R. 3d at 14). This significant facet of the *Signal* opinion was entirely misunderstood by the court below for it plainly erred in saying (R. 658-659):

> "When the Signal Oil case was before the Commission, it said that the *justness and the reasonableness of the rate* was a 'vital element' in demonstrating 'that the service proposed is or will be required by the present or future public convenience and necessity.' Cities Service Gas Co., et al., 12 P.U.R. 3d 3, 14 (1955)." (Italics supplied.)

As quoted above, the Commission emphasized in *Tamborello* the necessity for a "conscientious appraisal of the evidence" in determining what disposition of a certificate case is required in the public interest. Application of that principle to the facts in this case required the conclusion reached by the Commission in its June 24 order.

c. *Proper Administration of the Act.*

The practical problems involved in the administration of the Natural Gas Act require that the Commission be

given a broad discretion in determining whether a certificate application is in the public convenience and necessity. If independent producer certificate cases are required to be turned into rate cases where the Commission must determine whether the proposed initial rate is "just and reasonable" under the standards provided in Sections 4 and 5 of the Act, it will be utterly impossible for the Commission to administer the Act.[21] If such a burden is imposed upon the Commission, the supply of natural gas available to the interstate market will be severely limited because of the months, if not years, that will elapse before the Commission can determine whether each and every initial rate is justified.

The Commission has not yet formulated any definitive or workable standards for determining whether a producer's contract price meets the just and reasonable standards of the Act. Neither the Commission nor the producers know what criteria of proof is required. *Forest Oil Corp.* v. *FPC*, (5th Cir., decided February 20, 1959). Compounding the complexities already inherent in a Section 7 certificate proceeding with the so far insoluble difficulties of a rate proceeding will completely disrupt and delay the Commission's attempt to devise a workable regulatory pattern. The burden on the Commission will become intolerable, and the

[21] In 1958, 1,601 certificate applications were filed by independent producers, whereas a total of 1,395 were disposed of during the year. This leaves 2,024 certificate applications pending at the end of the year compared with 1,818 on hand a year earlier. Since June 7, 1954, 10,761 certificate applications have been filed and 8,737 have been disposed of, most of these in uncontested proceedings. On the other hand, during the year 1958, independent producers filed 1,939 rate increases. Of this amount, the Commission suspended 1,064. By comparison, there were 2,330 rate increases filed in 1957, of which 717 were suspended. At the end of 1958, the Commission had pending 2,034 increases. This compared with 1,040 increases which were pending at the end of 1957. At the end of 1956, there were only 358 suspensions pending. In addition to the 1,064 new suspensions issued in 1958, 16 other cases which the Commission had previously disposed of were remanded by the courts in 1958, leaving on hand 2,021 rate increase cases. On the other hand, during 1958, the Commission disposed of only 56 rate increases. FPC Press Release No. 10183, issued December 8, 1958.

additional delay between the time a contract for the sale of natural gas in the interstate market is executed and the time it is certificated will inevitably result to the detriment of all parties concerned, and the additional supplies of natural gas which the consuming public so vitally needs will be reduced to a mere trickle.[22]

It is evident that where the reasonableness of the proposed initial price is brought into issue, the Commission has a choice of remedies under the Act. In this case, the Commission decided to issue the certificate in accordance with the applicant's contract and determine the reasonableness of the initial rate in appropriate proceedings under Section 5 of the Act. This was a proper exercise of the Commission's discretion because responsibility for selecting the means of achieving the statutory policy and the relation of the remedy to that policy are matters peculiarly within the Commission's discretion and should not be disturbed by the courts on appeal. *American Power & Light Co.* v. *SEC*, 329 U.S. 90 (1946); *Phelps Dodge Corporation* v. *NLRB*, 313 U.S. 177, 194 (1941); *General Protective Com.* v. *SEC*, 346 U.S. 521, 534 (1954).

2. The Commission's June 24 Order Is Supported by Substantial Evidence.

The Commission's June 24 order is predicated upon its determination that "in view of the great demand for gas by customers of Tennessee Gas, the price consideration should not be made the prime determinant of what the public convenience and necessity require" (R. 487). In this

[22] It is significant to note that the Commission has not yet completed its investigation as to the reasonableness of the natural gas rates of Phillips Petroleum Co. In fact, the matter is still pending before the Presiding Examiner. Docket Nos. G-1148, et al. The Court will recall that this proceeding was the basis for its decision in *Phillips Petroleum Co.* v. *State of Wisconsin*, 347 U.S. 672 (1954).

regard it is significant to note that the need for this gas is uncontroverted. The numerous certificates previously issued to Tennessee leave no doubt as to its ever-present need for additional supplies of gas to satisfy the insatiable demands of its ever-expanding market.[23] The Commission could not properly ignore the increasing consumption of gas by Tennessee's present customers and the many thousands of additional consumers in the areas served by Tennessee that will be served as a result of this purchase (R. 487). In fact, as indicated by this Court, concern for the ultimate consumer is a primary consideration under the Natural Gas Act.[24]

Nor can the advantages to Tennessee, and thus to the ultimate consumers, that will result from the certification of the proposed sales be overlooked. Summarized, these advantages are (R. 46-47, 250-251):

(1) A good location with respect to Tennessee's main transmission system;

(2) A large amount of gas reserves proven at the time of negotiation (1,673,929,000,000 cubic feet of natural gas have been proven on 11,500 of the 95,000 dedicated acres);

(3) A great potential for additional reserves within the dedicated acreage, which will be available to Tennessee in the future;

(4) An entry afforded into other vast areas of prolific offshore reserves, thereby placing Tennessee in a favorable position to acquire additional reserves developed in the future and enabling it thereby to continue to meet the expanding demands of its customers; and

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[23] Tennessee serves customers in the states of Tennessee, Ohio, Pennsylvania, New York, Massachusetts and other New England states. The growth in the consumption of natural gas in those states during recent years has been tremendous and it is expected to increase in the future.

[24] *FPC* v. *Interstate Natural Gas Co.*, 336 U.S. 577, 581 (1949); *Phillips Petroleum Co.* v. *State of Wisconsin*, 347 U.S. 672 (1954); *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944).

(5) Acquisition of reserves which constituted the only large gas reserve for sale at that time in the Gulf Coast area.

The impact of these factors on Tennessee's ability to continue to meet the need of its ultimate consumers clearly indicates that the proposed sales were required by the public convenience and necessity. The June 24 order reflects an exercise of the Commission's function not only to appraise the facts and draw inferences from them, but also to bring to bear upon the problem an expert judgment and to determine from an analysis of the total situation on which side of the controversy the public interest lies. *United States* v. *Detroit & Cleveland Nav. Co.*, 326 U.S. 236, 241 (1945).

The Commission's decision not to make price the prime determinant is further supported by the fact that there have been no other sales of gas in West Cameron, East Cameron or Vermilion offshore areas prior to this sale (R. 43-44). In fact, there is no evidence of any offshore sale within 200 miles of any lease involved in these proceedings (R. 58). Since these leases are not in any of Tennessee's Louisiana pricing districts, the proposed sales will not cause economic disruption of existing price structures and will not "trigger" favored-nation or price-redetermination clauses in other contracts (R. 43, 148-159). Nor will the proposed price cause Tennessee to request an increase in its rates (R. 202).

An applicant under Section 7(e) of the Act who shows that he is able and willing to perform the service proposed and that such service is or will be required by the present or future public convenience and necessity is entitled to a certificate as a matter or right. The record in this case firmly establishes without dispute that the Producers are ready and willing to perform their obligations under their contracts with Tennessee. The Produc-

ers have dedicated leases covering over 95,000 acres to the performance of their contracts with Tennessee, and although only 12 per cent of this dedicated acreage has been developed, the already proven recoverable reserves are 1.673 trillion cubic feet (R. 143). At the time of hearing, 22 gas wells had been completed in water as deep as 90 feet, and 11 additional wells were programmed for the balance of 1957 (R. 25). The full extent of this prolific gas reserve has not yet been determined, but the 12 per cent of the leases which has been developed represented the largest single sale of gas available on the Gulf Coast and will constitute 11 per cent of the total gas supply of Tennessee (R. 41, 139-140). The evidence further showed that each of the Producers was financially and technically able to do all things necessary to perform their obligations (R. 27-29). These uncontroverted facts clearly demonstrate that the Producers met the prerequisites prescribed in Section 7 of the Act and the Commission properly granted them certificates pursuant to their contracts with Tennessee (R. 570-571).

The Commission has recently summarized what it considers to be the requirements for a *prima facie* case by an independent producer in a certificate proceeding as follows:

> "We are of the view that if the applicant proves there is a market for the gas at the proposed price and that the project is economically feasible at the proposed price (both market and economic feasibility being factors which we consider in determining public convenience and necessity) that it has sustained its burden of going forward with the evidence, and in the absence of evidence showing that the proposed price or rate adversely affect the public convenience and necessity, the applicant has made out a *prima facie* case, and a certificate should issue to it."[25]

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[25] *Re Hope Natural Gas Company*, Docket No. G-12571, issued March 31, 1958.

Here, there is no question that there is a market for the Producers' gas and that the project is economically feasible at the initial price. There was introduced no evidence of any kind showing that such price would adversely affect the public convenience and necessity. On the contrary, the record discloses that no other contract prices will be affected and that Tennessee will not be required to seek a rate increase (R. 43, 202). Accordingly, the Producers have established a *prima facie* case, and the foregoing evidence forms substantial support for the Commission's June 24 certification of the sales proposed by the Producers. It was incumbent upon the court below to sustain this proper exercise of the Commission's discretion.[26]

II

THE PRODUCERS' REFUSAL TO ACCEPT CONDITIONAL CERTIFICATES DID NOT DEPRIVE THE COMMISSION OF AUTHORITY, ON REHEARING, TO ISSUE UNCONDITIONAL CERTIFICATES.

1. The Producers Had the Contractual and Statutory Right To Reject the Conditional Certificates Contained in the May 20 Order.

Respondents argued below that the June 24 order constituted an abuse of discretion by the Commission because the Commission had concluded in its earlier orders of April 22 and May 20 that the record did "not contain sufficient evidence on which to base a finding that the public convenience and necessity requires the sale of the gas" at the contract rate level. They attributed the difference between

[26] Section 19(b), 52 Stat. 831 (1938), 15 U.S.C. 717r(b) (1952); Administrative Procedure Act, Section 10, Act of June 11, 1946, 60 Stat. 243, 5 U.S.C. 1009 (1952); *SEC* v. *Chenery Corporation*, 332 U.S. 194, 207 (1947); *ICC* v. *Parker*, 326 U.S. 60, 65 (1945).

the May 20 order and the final order to the Commission's submission to the so-called "threats" of the Producers to withhold their gas from the interstate market unless they received their initial contract price. Respondents urged that the Commission should attach a rate reducing condition to any certificate issued to the Producers, suggesting a wide variety of initial prices, reasons and conditions.[27]

The court below expressly rejected the formulation of issues presented by Respondents and substituted a new objection of its own, not theretofore urged by any party, saying (R. 658):

> "* * * We conceive of the question, however, as a more fundamental one, involving the statutory jurisdiction of the Federal Power Commission. It is whether the Commission has authority to consider an application for a certificate under Section 7(c) where the terms of the application limit the scope of the inquiry which the Commission is required to make for a determination of public convenience and necessity."

In support of its conclusion that the Commission did not have statutory authority to consider the Producers' applications, the court relied upon statements by the Commission in its earlier orders of April 22 and May 20 that the

[27] It was contended that the Commission should investigate the initial rates to determine whether they were "within the ball park" (Long Island Lighting Br. 12, 16), or that the rates are "within reasonable range of a 'just and reasonable' price" (id. 13), or that "an inquiry should be made 'at least if the price appears to be out of line'" (id. 13-14). PSC claimed that the Commission should have attached a condition reducing the initial rate "to a level which would be without deleterious effect upon the interstate market, the interstate pipelines, and, through them, the ultimate interstate consumers" (PSC Br. 19). Public Service suggested that the Commission should require a showing that "the contracted rate level or price was required or needed by the applicants" (Public Service Br. 5). It argued further that the Commission should require applicants to present evidence of "operating expense, capital costs or profits" or that the contract rate is "necessary to insure confidence in their financial integrity or to maintain credit or attract capital" (id. 11). At best, these arguments constitute no more than claims for an exercise of Commission discretion different from that which it found to be required by the public convenience and necessity.

record contained insufficient evidence on which to base a finding that the sale at the contract rate would be in the public interest (R. 659-660). From this, the court concluded that decisions by the Producers not to accept the certificates tendered in the May 20 order constituted "threats" which limited the scope of the Commission's inquiry and deprived it of jurisdiction to consider further the Producers' applications.

A "threat" is an "expression of an intention to inflict loss or harm on another by *illegal* means" (italics supplied).[28] Connotations adverse to the Producers thus result from the repeated misuse by the court below of the term "threat" (R. 657, 660) to describe the undeniable *legal* right of the Producers to commit, or decline to commit, their reserves to interstate service under a proffered certificate.[29] This misunderstanding by the court, which is basic to its decision, is a misconception that Section 7 of the Act requires an applicant to agree in advance to accept any certificate which might be issued to it.

The applications of the Producers contained no unusual provisions or conditions, and followed the requirements of the Commission's regulations.[30] In conformity with these regulations, copies of the contract of each Producer were attached to the various applications (R. 19-21). Each contract provided that certificates of public convenience and necessity *satisfactory* to both the Producers and to Tennessee must be received, or the contracts were subject to cancellation (R. 28, 287-288). Such provisions are cus-

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[28] Webster's New International Dictionary, 2nd ed., G. & C. Merriam Company (1955).

[29] For example, the court said (R. 660):

"It was only after the threat of withholding the gas from interstate market that the Commission retreated from its previous position and granted the certificates without rate conditions by its order of June 24, 1957."

[30] 18 C.F.R. 157.24-157.25.

tomary in gas purchase contracts. The Producers, in refusing to accept the May 20 order, did no more than exercise the right given them under their contracts to refuse to accept an unsatisfactory certificate. Furthermore, such right of rejection is recognized in the Commission's regulations.[31] Indeed, each of the orders issued by the Commission in this proceeding contains clauses providing for acceptance thereof by the Producers (R. 489, 608, 617). Their refusal to accept an unsatisfactory certificate could not oust the Commission of jurisdiction to consider the matter further.

A request for a certificate which simply allows a producer to carry out the terms and provisions of his contract, including the initial rate at the level provided for in such contract, is in accordance with the plain provisions of the Natural Gas Act and in no sense ousts the Commission of jurisdiction to consider further the certificate application. Under the Natural Gas Act, all rates are established originally by private parties, and the Commission's sole function is to review these rates. This dichotomy between the rate-setting and rate-reviewing powers of the Commission was firmly established in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956), where Mr. Justice Harlan, speaking for the Court, said:

> "In construing the Act, we should bear in mind that it evinces no purpose to abrogate private rate contracts as such. To the contrary, by requiring contracts to be filed with the Commission, the Act expressly recognizes that rates to particular customers may be set by individual contracts. In this respect, the Act is in marked contrast to the Interstate Commerce Act, which in effect precludes private rate agreements by its requirements that the rates to all shippers be made

[31] 18 C.F.R. 157.20.

uniform, a requirement which made unnecessary any provision for filing contracts. * * * Recognizing the need these circumstances create for individualized arrangements between natural gas companies and distributors, the Natural Gas Act permits the relations between the parties to be established initially by contract, the protection of the public interest being afforded by supervision of the individual contracts, which to that end must be filed with the Commission and made public.

* * *

"* * * Moreover, the very premise that Sections 4(d) and (e) and 5(a) are alternatively rate-changing 'procedures' is itself based on a misconception of the structure of the Act. These sections are simply parts of a single statutory scheme under which all rates are established initially by the natural gas companies, by contract or otherwise, and all rates are subject to being modified by the Commission upon a finding that they are unlawful. The Act merely defines the review powers of the Commission and imposes such duties on natural gas companies as are necessary to effectuate those powers; it purports neither to grant nor to define the initial rate-setting powers of natural gas companies.

"The powers of the Commission are defined by Sections 4(e) and 5(a). The basic power of the Commission is that given it by Section 5(a) to set aside and modify any rate or contract which it determines, after hearing, to be 'unjust, unreasonable, unduly discriminatory, or preferential'. This is neither a 'rate-making' nor a 'rate-changing' procedure. It is simply the power to review rates and contracts made in the first instance by natural gas companies and, if they are determined to be unlawful, to remedy them.

* * *

"* * * In short, the Act provides no 'procedure' either for making or changing rates; it provides only for

notice to the Commission of the rates established by natural gas companies and for *review* by the Commission of those rates. The initial rate-making and rate-changing powers of natural gas companies remain undefined and unaffected by the Act.

"All of the relevant provisions of the Act can thus be fully explained as simply defining and implementing the powers of the Commission to review rates set initially by natural gas companies, and there is nothing to indicate that they were intended to do more. Admittedly, the Act presumes a capacity in natural gas companies to make rates and contracts and to change them from time to time, but nowhere in the act is either power defined. The obvious implication is that, except as specifically limited by the Act, the rate-making powers of natural gas companies were to be no different from those they would possess in the absence of the Act: to establish ex parte, and change at will the rates offered to prospective customers; or to fix by contract, and change only by mutual agreement, the rate agreed upon with a particular customer."

Mobile concretely establishes that under the Natural Gas Act the initial "rate-setting powers" remain vested in private parties and that the Commission's sole function is to review the rates set in the first instance by such parties. The Commission's review function was recently reaffirmed in *United Gas Co.* v. *Memphis Gas Div.*, 358 U.S. 103 (1958), where Mr. Justice Harlan, again speaking for the Court, stated:

"Thus, Mobile, properly understood, affirmatively establishes United's right to proceed under Section 4 in the circumstances of this case. As we there said, 'the initial rate-making and rate-changing powers of natural gas companies remain undefined and unaffected by the Act.' 350 U.S. at 343."

Here, all that the Producers did was to refuse to accept proffered certificates which would have deprived them of their initial rate-setting powers. The Producers had the undeniable legal right to accept or reject the certificates, and there is nothing in the Act that requires an applicant to agree in advance to accept any certificate which might be issued to it.

The rate-changing powers of the Commission are contained in Sections 4 and 5 of the Act. After a hearing conducted under the auspices of either of these sections, the Commission can change a rate established by the parties. The Commission properly recognized this in its June 24 order by relegating the determination of the reasonableness of the Producers' rates to a Section 5 proceeding.

As noted above, Section 7 of the Act delineates the Commission's functions with respect to certificate applications. It is true that Section 7(e) grants the Commission authority to attach "reasonable conditions." However, if that authority be employed in an effort to impose a Commission-determined rate so as to force an applicant to undertake the sale at the Commission-fixed price, there is an undeniable collision with the limitations on the Commission's rate powers as detailed in *Mobile*. Yet that is precisely the effect of the decision below. Clearly, the imposition of a rate condition which an applicant is required to accept is beyond the power of the Commission under Section 7. In this manner the Act can be construed as a single statutory scheme of regulation which affords a reasonable accommodation between the conflicting interests of contract stability on the one hand and public regulation on the other, and Sections 4, 5 and 7 of the Act are reconciled so as to produce a symmetrical whole. *FPC* v. *Panhandle E. P. L. Co.*, 337 U.S. 498, 514 (1949); *Panhandle Eastern Pipe Line Co.*

v. *FPC*, 204 F. 2d 675 (3rd Cir., 1953); *Central West Utility Co.* v. *FPC*, 247 F. 2d 306, 313 (3rd Cir., 1957).

An applicant's right to reject a conditional certificate is reinforced by the legislative history of the Act, which shows that it was anticipated that an applicant might either reject a tendered certificate or apply for rehearing because of a condition it deemed unduly burdensome. Commissioner Manly, testifying with respect to the 1942 amendment of Section 7, stated:[32]

> "*Commissioner Manly* * * * Now, what the Commission does under ordinary conditions is to require those conditions to be set forth in the authorization for a certificate that is accepted by the company as a condition precedent to the actual issuance of the certificate, so that in all intents and purposes the company has a right to reject a certificate containing any conditions which are unreasonable, onerous, or have no relevancy to the issue.
>
> "*Mr. South*: That is what I have in mind. If they are too burdensome, then the application could be withdrawn.
>
> "*Commissioner Manly*. They could come back before the Commission and ask for a rehearing if they regard the terms and conditions as being onerous."

It cannot be said, as the court below put it, that the Producers' request for certificates conforming to their contracts implied a "condition" to their applications "requiring the Commission to forego consideration of an element which may be necessary in the formulation of its judgment" (R. 662). For such a request does no more than present the nature of the proposal of the Producers to be weighed

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[32] Hearings before the House Committee on Interstate and Foreign Commerce on H. Rep. No. 5429, 77th Cong., 1st sess., p. 23 (1941).

by the Commission against the totality of the requirements of public convenience and necessity. In addition, even if this were not so, the court below erred in supposing that a conditional application could "limit" the statutory jurisdiction of the Commission. Cf. *Sunray Mid-Continent Oil Company* v. *FPC*, 239 F. 2d 97 (10th Cir., 1956), rev'd on other grounds, 353 U.S. 944 (1957). The Producers' request for a certificate allowing them to carry out the terms and provisions of their contracts and to approve the initial rate at the level provided for in the contract, in no sense ousted the Commission's jurisdiction to consider the proposal. Nor did it in any way limit the Commission's inquiry into the price aspects of the proposal, along with other elements entering into the complex of public convenience and necessity.

2. The Commission Had the Authority To "Change Its Mind."

Obviously, on rehearing, the Commission had the authority to change its mind and issue the order of June 24. The lower court could not properly concern itself with alleged inconsistent findings made in the prior orders of April 22 and May 20. *Virginia Ry. Co.* v. *U. S.*, 272 U.S. 658, 665-666 (1926). Section 19(a) of the Act confers the right to seek rehearing of a final order of the Commission. It not only authorizes application for rehearing, but empowers the Commission "to grant or deny rehearing or to abrogate or modify its order without further hearing."[33] Without this power, of course, the granting of a rehearing would be an empty gesture. Manifestly, Section 19(a) contemplates the possibility of the reaching of a different result without additional evidence. On rehearing, if the Commis-

[33] 52 Stat. 821 (1938), 15 U.S.C. 717r(a) (1952).

sion does change its mind, the reviewing court must concern itself solely with the question of whether the final order under review is supported by substantial evidence. Thus, in *Cia Mexicana de Gas* v. *FPC*, 167 F. 2d 804 (5th Cir., 1948), the court considered a Commission order granting an export permit, which order reversed, after rehearing, a prior order denying such permit. Upholding the Commission's final order, the court stated (167 F. 2d at 806):

> "The fact, of which petitioners seek to make so much, that on the first hearing the Commission, two commissioners dissenting, refused the permit, and on the second hearing, without substantial additional evidence, granted it, is, we think, without significance here. A commission, like a court, may, indeed should, change its findings and order if on rehearing it is of a different mind. If it does so change, our function on a review of its findings and order is to determine not which of the two findings and orders was the best but whether, as claimed by petitioners, the findings and order under review are without evidence to support them."

A similar result was reached in *National Coal Association* v. *FPC*, 247 F. 2d 86 (D.C. Cir., 1957), where the court upheld a Commission order which without additional evidence reversed an earlier order issued in the same proceeding. The court stated (247 F. 2d at 88):

> "Since the order under review was based on findings sustained by evidence, and since we perceive no procedural error prejudicial to petitioners, we are not authorized to interfere with the Commission's evaluation of the public interest, the making of which is committed to its judgment."

This same rationale applies with full force here. It is immaterial that the Commission changed its mind in eval-

nating the public interest—a function committed to its judgment. Moreover, a Commission order is presumptively valid, and the Commission will be presumed to have properly performed its official duties. *Baltimore & O. R. Co.* v. *United States*, 298 U.S. 349, 358-359 (1936).

The court below recognized that the Commission had the authority "to change its mind"[34] but held that the June 24 order was not a proper exercise of this authority because: (1) the Commission dispensed with the consideration of the price element;[35] (2) conditions attached to the Producers' certificate applications limited the Commission's inquiry; and (3) the Producers were unwilling to conform to the conditions of the Act.[36] In so holding, the court has disregarded the plain language of the June 24 order, the content of the Producers' certificate applications and the uncontroverted evidence in the record.

First, the June 24 order clearly reflects that the element of price was thoroughly considered by the Commission in reaching its final decision. Significantly, the court below does not even mention the extensive discussion of the initial price contained in the June 24 order (R. 568-570), but

[34] The court stated (R. 661):

"Since in its first two orders the Commission determined that the record lacked sufficient evidence upon which to base a finding that the sale at the proposed rate would be in the public interest, and as the final order was based upon the same record, there is still insufficient evidence to support such a necessary finding."

[35] The court averted to the Commission's authority to consider price and then said (R. 662):

"In the present case, that the initial rate was a necessary consideration in the scope of inquiry into the determination of public convenience and necessity has been twice recognized by the Commission, even to the extent that its order of May 20, 1957, in fact conditioned the permanent certificates upon a contract amendment as to the initial price."

[36] In direct controvention of the Commission's formal findings (R. 489), which are unchallenged and binding because supported by substantial evidence, the court below stated (R. 662):

"The action of the applicants in curtailing the decision-making power of the Commission demonstrates their unwillingness to conform to the provisions of the Act; this in itself would require the denial of the applications."

relies solely on the Commission's earlier orders which are not under review and which had been abandoned by the Commission in its search for a decision best serving the public interest. Admittedly, these earlier orders also considered the price element, but that fact does not alter the unequivocal language of the June 24 order which discloses that the initial price was considered in the Commission's determination of the public convenience and necessity.

It is simply not true that any conditions were attached to the applications involved, either in fact or by implication. The Producers' applications were in the customary form and judicially met all applicable requirements.[37] The Commission did not conduct a "limited inquiry" in any sense but, as reflected by the June 24 order, considered the entire ambit of elements comprising the public convenience and necessity. The fact that the court below might have conducted the inquiry differently does not justify its reversal of the June 24 order. *United States* v. *Detroit & Cleveland Nav. Co.*, 326 U.S. 236, 241 (1945); *Department of Conservation of Louisiana* v. *FPC*, 148 F. 2d 746, 750 (5th Cir., 1945). Obviously the Producers could not and did not curtail the decision-making power of the Commission.

It is impossible to point to any provision of the Act to which the Producers were unwilling to conform or to show that they have not complied precisely with the requirements applicable to the submission of certificate applications by Producers.[38] On the contrary, there is unchallenged evidence in the record to support the Commission's findings that the Producers were willing to conform to the Act and the regulations thereunder (R. 570). Apparently, the court below erroneously assumed that the mere filing of the cer-

[37] See Section 7(d), 56 Stat. 84 (1942), 15 U.S.C. 717f(d) (1952), and 18 C.F.R. 157.23-157.31.

[38] 18 C.F.R. 157.23-157.31.

tificate applications somehow required the Producers to accept whatever certificates were eventually issued to them. Only such a misunderstanding could give rational meaning to the court's use of the term "threat" to describe the legal refusal by the Producers to commit their reserves upon terms different from those contained in their contracts.

The Commission was authorized by Section 19(a) to reconsider and review its prior orders and upon reevaluating the complex of factors inherent in determining the public convenience and necessity, to issue the June 24 order. The fact that such action was taken in light of the Producers' decision to exercise their contractual right of cancellation did not affect the Commission's authority. Such considerations are completely immaterial to the determinative issue in this case—whether the June 24 order is a proper exercise of the administrative discretion vested in the Commission under the Natural Gas Act which is adequately supported by substantial evidence. Consideration of this fundamental issue marked the proper limit of judicial inquiry in reviewing the Commission's June 24 order.

III

THE COURT OF APPEALS ERRONEOUSLY PREDICATED ITS DECISION UPON A SUA SPONTE DETERMINATION OF THE COMMISSION'S AUTHORITY UNDER THE NATURAL GAS ACT.

Reversal of the decision below is independently required because of a clear violation by the Court of Appeals of the express limits on its reviewing authority.

The power of a court of appeals to review an order of the Federal Power Commission is limited strictly by Section

19(b)[39] of the Act which contains the "distinctive formulation of the conditions under which resort to the courts may be made and Congress determines the scope of jurisdiction of the lower Federal courts." *FPC* v. *Pacific Power & Light Co.*, 307 U.S. 156, 159 (1939). Section 19(b) of the Act limits the objections to be considered by the reviewing court as follows:

> "No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure to do so."

The decision rendered by the court below expressly rejects the errors urged by Respondents as to abuse of discretion. Instead, the court relies entirely upon its determination that because the Producers refused to accept certificates conditioned on an initial price lower than had been agreed upon in their contracts, the Commission was automatically deprived of authority to reconsider their certificate applications and to issue its June 24 order (R. 658, 662). No question as to jurisdiction[40] of the Commission was urged by any party on application for rehearing or otherwise while this matter was pending before the Commission or before the Court of Appeals. Thus, the decision rendered below is a flagrant disregard of the statutory limit on judicial review.

The unequivocal limitation upon the power of judicial review contained in Section 19(b) was emphatically en-

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[39] 52 Stat. 831 (1938), 15 U.S.C. 717r(b) (1952).

[40] The basis for the decision of the Court of Appeals was not a total lack of jurisdiction such as would be the case if an administrative agency other than the Federal Power Commission had issued Producers a Section 7(c) certificate. Rather here, the Court determined *sua sponte* that the jurisdiction of the Federal Power Commission had not been properly invoked because of the Producers' refusal to accept an initial rate lower than that specified in their contracts.

forced in *FPC* v. *Colorado Gas Co.*, 348 U.S. 492, 498-499 (1955), where this Court condemned the consideration of an objection which had not been urged before the Commission, holding:

> "Respondent's second and principal contention is that, although its application did not meet the requirements of Section 19(b) and *it* therefore is barred from attacking the validity of the merger conditions in the Court of Appeals, nothing precludes that court itself from raising, considering and sustaining the same objection, sua sponte. Respondent's error appears on the face of the statute. Section 19(a) first precludes the *bringing* of any proceeding in a Court of Appeals to review an order of the Commission, *unless the person bringing it previously has applied to the Commission for a rehearing on that order.* Section 19(b) then expressly precludes the *consideration* by the court of any objection to an order of the Commission, *unless the objection shall have been urged before the Commission in the application for rehearing.* As the court is thus expressly *precluded from considering* an objection when, without prior application to the Commission, that objection is presented to the court by the party directly aggrieved, it cannot be assumed that Congress intended to *permit* the same court to consider the same objection, under the same circumstances, sua sponte, merely because the objection was *not* presented to the court by the party aggrieved. Section 19(b) reflects the policy that a party must exhaust its administrative remedies before seeking judicial review. To allow a Court of Appeals to intervene here on its own motion would seriously undermine the purpose of the explicit requirements of Section 19(b) that objections must first come before the Commission." (Court's italics.)

See also, *American Power & Light Co.* v. *SEC*, 141 F. 2d 606 (1st Cir., 1944), aff'd, 329 U.S. 90 (1946); *Magnolia Petroleum Co.* v. *FPC*, 236 F. 2d 785, 789 (5th Cir., 1956);

Memphis Light, Gas & Water Division v. *FPC*, 243 F. 2d 628, 632 (D.C. Cir., 1957).

The *American Power and Light Company* case, *supra*, is striking in points of similarity with the situation here. There, the Securities and Exchange Commission, pursuant to Section 11(b)(2) of the Public Utility Holding Company Act,[41] had issued orders requiring dissolution of two subsidiaries of Electric Bond & Share Company. Review was sought pursuant to Section 24(a) of the Public Utility Holding Company Acts,[42] which is substantially identical with Section 19(b) of the Natural Gas Act. Petitioners sought to raise on review, for the first time, a question of whether Section 11(b)(2) authorized the dissolution of subholding companies as one method of bringing a holding-company system into compliance. The court held that it had no power to review the question, stating (141 F. 2d at 613):

> ". . . there can be no doubt that under §24(a) Petitioners were obliged to raise before the Commission issues as to the *Commission's statutory authority* to issue the contemplated orders." (Italics supplied.)

In one respect, our case differs, and this lies in the fact that here it was the court below which first raised the issue of the Commission's statutory authority. Further, this statutory limitation has been applied to a reviewing court's authority, even where matters of the Commission's jurisdiction are involved. In *Panhandle Pipe Line Co.* v. *FPC*, 324 U.S. 635, 649-651 (1945), this Court held that the company's failure in its application for rehearing to question the Com-

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41 Section 11(b)(2) of the Act of August 26, 1935, 49 Stat. 820 (1935), 15 U.S.C. 79k(b)(2) (1952).

42 Section 24(a) of the Act of August 26, 1935, 49 Stat. 834 (1935), as amended, 15 U.S.C. 79x (1952).

mission's jurisdiction to include producing properties in its rate base precluded the reviewing court's consideration of that question.

The decision of the court below should be reversed, if for no other reason, because the court transgressed the statutory limits on its reviewing authority.

CONCLUSION

WHEREFORE, for all the foregoing reasons, the judgment of the Court of Appeals should be reversed.

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March 9, 1959